Calendar No. 36

107TH CONGRESS *1st Session*	SENATE	REPORT 107–15

THE PUBLIC UTILITY HOLDING COMPANY ACT OF 2001

R E P O R T

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

TO ACCOMPANY

S. 206

together with

ADDITIONAL VIEWS

MAY 9, 2001.—Ordered to be printed

U.S. GOVERNMENT PRINTING OFFICE
89–010 WASHINGTON : 2001

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

PHIL GRAMM, Texas, *Chairman*

RICHARD C. SHELBY, Alabama
ROBERT F. BENNETT, Utah
WAYNE ALLARD, Colorado
MICHAEL B. ENZI, Wyoming
CHUCK HAGEL, Nebraska
RICK SANTORUM, Pennsylvania
JIM BUNNING, Kentucky
MIKE CRAPO, Idaho
JOHN ENSIGN, Nevada

PAUL S. SARBANES, Maryland
CHRISTOPHER J. DODD, Connecticut
TIM JOHNSON, South Dakota
JACK REED, Rhode Island
CHARLES E. SCHUMER, New York
EVAN BAYH, Indiana
ZELL MILLER, Georgia
THOMAS R. CARPER, Delaware
DEBBIE STABENOW, Michigan
JON S. CORZINE, New Jersey

WAYNE A. ABERNATHY, *Staff Director*
STEVEN B. HARRIS, *Democratic Staff Director and Chief Counsel*
LINDA L. LORD, *Chief Counsel*
STACIE THOMAS, *Economist*
DEAN V. SHAHINIAN, *Democratic Counsel*
GEORGE E. WHITTLE, *Editor*

CONTENTS

Calendar No. 36

107TH CONGRESS *1st Session* | SENATE | REPORT 107–15

THE PUBLIC UTILITY HOLDING COMPANY ACT OF 2001

MAY 9, 2001.—Ordered to be printed

Mr. GRAMM, from the Committee on Banking, Housing, and Urban Affairs, submitted the following

REPORT

together with

ADDITIONAL VIEWS

[To accompany S. 206]

The Committee on Banking, Housing, and Urban Affairs to which was referred the bill (S. 206), to repeal the Public Utility Holding Company Act of 1935, to enact the Public Utility Holding Company Act of 2001, and for other purposes, having considered the same, reports favorably thereon and recommends that the bill do pass.

INTRODUCTION

On April 24, 2001, the Senate Committee on Banking, Housing, and Urban Affairs met in legislative session and marked up and ordered to be reported S. 206, a bill to repeal the Public Utility Holding Company Act of 1935 ("PUHCA") and to enact the Public Utility Holding Company Act of 2001, and for other purposes, with a recommendation that the bill do pass. The Committee adopted by unanimous consent an amendment sponsored by Senator Enzi, and adopted by voice vote an amendment in the second degree to that amendment sponsored by Senators Enzi and Sarbanes. The Committee also adopted by voice vote an amendment sponsored by Senator Corzine. The Committee's action to report the bill was taken by a recorded vote. All Senators, except for Senator Stabenow, voted in the affirmative. Senator Stabenow voted in the negative.

HISTORY OF THE LEGISLATION

The Public Utility Holding Company Act of 2001, S. 206, was introduced on January 30, 2001 by Senators Shelby, Murkowski, Gramm, Dodd, Sarbanes, Lott, Craig and Crapo. Senators Brownback, Cochran, Bunning and Nickles were added as additional cosponsors. The legislation introduced was substantively identical to S. 313, the "Public Utility Holding Company Act of 1999," which was reported by the Banking Committee on February 11, 1999.[1] S. 206 has two purposes: first, to repeal the Public Utility Holding Company Act of 1935; and second, to put in place a new regulatory structure that allows for greater geographic and business diversification in the utility industry while ensuring that utility customers do not pay for this diversification through increased energy rates.

The full Committee conducted a legislative hearing to consider S. 206 on March 29, 2001. The Committee received testimony from: the Honorable Isaac Hunt, Jr., Commissioner, Securities and Exchange Commission ("SEC"); Cynthia A. Marlette, Deputy General Counsel, Federal Energy Regulatory Commission ("FERC"); David L. Sokol, Chairman and CEO, Mid-American Energy Holdings Company; David M. Sparby, Vice President, Government and Regulatory Affairs, Xcel Energy Inc.; and Charles A. Acquard, Executive Director of the National Association of State Utility Consumer Advocates ("NASUCA").

PURPOSE AND SUMMARY

The bill reported by the Committee would repeal PUHCA. In the 66 years since PUHCA became law, the nature of the utility industry changed, state and Federal governments implemented regulatory controls, and Congress enacted federal energy laws and Federal securities laws—all of which now more than adequately protect consumers and utility rate payers. In light of these developments, PUHCA no longer serves its original purpose of restructuring the energy industry and protecting investors and consumers from holding company abuses and has become obsolete. As the SEC—the Federal agency that enforces PUHCA—has testified, PUHCA "has become redundant in many respects, as a result of prudent administration of the statute and the development and evolution of other state and Federal regulation."[2] Therefore, "the SEC has recommended, and continues to recommend, that Congress repeal the 1935 (PUHCA) Act."[3]

The Committee recognizes that repealing PUHCA not only streamlines regulation, but would also facilitate efforts to achieve competitive markets in the energy industry. Truly competitive energy markets are going to require significant capital investment. However, PUHCA inhibits investment and precludes financially sound firms from participating in the energy markets. It is the Committee's view that repealing PUHCA would attract new market

[1] Only technical changes were made to the text of S. 313 prior to the bill being reintroduced as S. 206 in the 107th Congress.

[2] Statement of Isaac C. Hunt, Jr., Commissioner, Securities and Exchange Commission: "Hearing on the Public Utility Holding Company Act of 2001," Senate Committee on Banking, Housing, and Urban Affairs, Subcommittee on Securities and Investment, March 29, 2001 at 2.

[3] Id. at 5.

participants, stimulate investment, and ultimately engender greater competition to the benefit of consumers.

Perhaps most importantly, S. 206 would provide for additional consumer protections by enhancing regulatory oversight of the ratemaking process. The Committee believes that the regulators must be able to ensure that consumers pay only for costs associated with utility services. S. 206 does not in any way diminish the authority provided to the FERC by the Federal Power Act to protect ratepayers. In fact, S. 206 would expand the existing ratemaking authority of Federal and state energy regulators by allowing them to review the records of utility transactions in order to protect ratepayers from unfair rate increases and any abusive practices.

The bill would also allow the FERC and the states to more effectively protect ratepayers by addressing a problem created by the decision of the Court of Appeals for the District of Columbia Circuit Court in *Ohio Power Company* v. *FERC*[4] ("*Ohio Power*"). The court in *Ohio Power* held that the FERC did not have authority to regulate certain costs in setting utility rates when those costs had previously been approved by the SEC. The *Ohio Power* decision also puts into question the states' ratemaking authority. S. 206 would remove the SEC from the ratemaking process and establish that the FERC (and implicitly the states) maintain full ratemaking authority.

S. 206 would ensure that regulators have the necessary authority to protect consumer rates by granting the FERC and the state public service commissions the authority to review a holding company's books and records, to the extent necessary to review rates. The legislation would give the FERC and state public utility commissions access to books and records of all utility holding companies, their associates, affiliates, and subsidiaries, that are relevant to the determination of rates.[5] The bill also contains an enforcement mechanism to ensure that the state commissions will be able to implement this newly expanded books and records review authority.

Due to some broader concerns raised about competition within the energy markets, the Committee adopted two amendments which call for studies of the markets. Specifically, S. 206 would establish an interagency task force composed of members from the Department of Justice, FERC, the Federal Trade Commission, the Department of Agriculture and the Securities Exchange Commission to study competition within the wholesale and retail markets for electric energy in the United States. The scope of the study is to encompass all retail and wholesale electric energy market participants. Additionally, the bill requires the Comptroller General to study the success of the Federal Government and the states in preventing anticompetitive practices, market-power abuses and promoting competition within the energy markets. Notwithstanding the Committee's interest in obtaining information about the condition of the national energy markets, the Committee continues to believe that the debate on comprehensive energy reform should be reserved for the Energy and Natural Resources Committee.

---

[4] *Ohio Power Company* v. *FERC,* 954 F.2d 779 (D.C. Cir. 1992).

[5] These provisions augment the existing books and records authority of both the FERC (as contained in the Federal Power Act, 16 U.S.C. 825) and the state commissions.

PURPOSE AND SCOPE

Background

The "unregulated" energy industry

In the early 1900's utility holding companies expanded rapidly—"fueled" by growth in the electric and gas industries and financing from Wall Street.[6] As a result of this rapid growth, industry power was concentrated among a handful of large interstate holding company systems.[7]

In the late 1920's, at Congress' request, the Federal Trade Commission ("FTC") undertook an extensive study of the public utility industry. At the conclusion of this seven year study, the FTC published a 107 volume report. The FTC report was followed by a second, two-year Congressional study. Both these studies uncovered a myriad of utility industry abuses facilitated by the holding company structure. These included the issuance of securities based on unsound assets, mismanagement and exploitation of subsidiaries, interaffiliate dealing, and the use of the holding company structure to evade effective regulation.[8]

The studies found that the utility holding companies' pyramidal corporate structure facilitated most of the industry abuses. Holding companies bought other holding companies—creating up to 10 layers of ownership between the utility subsidiary and its holding company. Since it was difficult to determine the true assets and liabilities of the company, this structure greatly increased the speculative nature of the holding companies' securities. The holding companies manipulated market rates for their securities and inflated their capital structure by forcing subsidiaries to buy supplies from affiliates at exorbitant above-market prices. The holding company structure made it virtually impossible to trace these abusive interaffiliate transactions. As a result of the abuses, investors were defrauded, subsidiary companies were forced to pay excessive prices for services, and in the end, energy prices were grossly inflated.

States were unable and ill-equipped to regulate these multistate holding companies effectively. At that time, many states did not have a utility-related regulatory structure in place and the Supreme Court considered state regulation of multistate holding companies a violation of the Commerce Clause of the Constitution.[9]

The new regulatory regime—The Public Utility Holding Company Act of 1935

Congress enacted the Public Utility Holding Company Act ("PUHCA"') in 1935 to remedy these holding company abuses. First, PUHCA mandated the simplification of the utility holding company structure. The break-up of the mammoth holding company systems was achieved by imposing an "integration requirement," which limited holding companies to owning only energy and

[6] SEC Study, "Regulation of Public Utility Holding Companies, Division of Investment Management," June 1999 ("SEC Study") at 1.
[7] Id. at 3.
[8] Id. at 3.
[9] Id. at 2.

energy-related companies in discrete geographic areas. Second, PUHCA gave the SEC authority to oversee these companies.[10]

Under this regulation, holding companies with multistate utility operations were required to register with the SEC and thus become subject to the full panoply of regulation imposed by PUHCA.[11] Prior SEC approval was required for certain corporate transactions engaged in by registered holding companies such as: securities issued, utility assets acquired, and some merger activities. Restrictions against interaffiliate loans and diversification into non-utility businesses were also imposed. PUHCA also subjected registered holding companies to extensive reporting and accounting requirements. As of December 31, 2000 there were 26 registered holding companies that own 214 electric and gas utility subsidiaries, with operations in 44 states, and in excess of 1,500 non-utility subsidiaries. Registered holding companies represent over 40% of the assets and revenues of the U.S. investor-owned electric utility industry, and almost 50% of all electric utility customers in the United States.[12]

The studies begin a twenty-year debate on PUHCA

Congress has debated the issue of PUHCA reform for nearly twenty years. The industry, the regulators, the Congress, and consumer and environmental protection groups agree that the SEC has completed its task—assigned over sixty-five years ago—of simplifying the utility holding company structure and that many of the remaining PUHCA provisions duplicate other Federal or state laws, or are unduly burdensome.

In 1977, the General Accounting Office (the "GAO") issued a report on the SEC's enforcement of PUHCA.[13] The GAO initiated the report in response to an inquiry from Congressman John Dingell, then Chairman of the Subcommittee on Energy and Power of the House Committee on Interstate and Foreign Commerce. The GAO reported that many of PUHCA's objectives had been met by the SEC's actions to reorganize and simplify the pyramidal corporate structures and that, as a result, financial conditions in the gas and electric utility industries had become more stable. Recognizing that Congress may need to reform PUHCA, the GAO included in its recommendations that the SEC undertake a complete study on PUHCA.[14]

The SEC recommended to Congress in 1981 that Congress repeal PUHCA: "on the basis that the reorganization of holding companies contemplated under [PUHCA] had been completed and that the remaining provisions were either duplicative of other regulatory schemes or no longer necessary to prevent the abuses that led to

---

[10] Id. at 7. The Congress determined that the SEC should oversee holding companies and PUHCA since the agency had "expertise in financial transactions and corporate finance." Id.

[11] Id. at 7, 8. The companies are referred to as "registered utility holding companies" since they come within the purview of PUHCA. At the time of the study, there were 19 registered holding companies. In 1932—three years before PUHCA became law—thirteen large holding companies controlled 75% of the electric utilities while eleven companies held over 80% of the gas pipelines. See, CRS Report, "The Public Utility Holding Company Act of 1935: Legislative History, Background and Recent Amendments," 93–266 A. at 2.

[12] Statement of Commissioner Isaac C. Hunt, Jr., supra note 2 at 3, n. 3.

[13] "The Force of The Public Utility Holding Company Act has Been Greatly Reduced by Changes in the Securities and Exchange Commission's Enforcement Policies." See, GAO Report to Congress FGMSD–77–35, June 20, 1977.

[14] Id. at 16, 17.

enactment of [PUHCA]."[15] Senator Alfonse D'Amato, (R–NY), then Chairman of the Securities Subcommittee of the Banking Committee, and Senator J. Bennett Johnston, (D–LA), then Ranking Member of the Energy Regulation Subcommittee of the Energy Committee, acted on the SEC's recommendation by introducing three separate bills to reform PUHCA. These measures sparked Congressional debate on PUHCA reform.[16] Senator D'Amato set the tenor of the debate in his statement introducing the legislation on the Senate floor. He said that PUHCA reform was necessary because "the Public Utility Holding Company Act is a major impediment to meaningful attempts to improve the economic well-being of the utility industry.[17]

In 1983, the GAO responded to the SEC's recommendations and to Senators D'Amato and Johnston's legislation by issuing yet another report on PUHCA. In this report, the GAO agreed that a number of PUHCA's provisions duplicated other laws. The GAO also identified regulatory gaps that would occur if PUHCA were repealed. For example, the report cited "approvals of acquisitions and financing of holding companies and the review of cost allocations between holding companies and their service companies and utility subsidiaries" as areas in which PUHCA provided the only authority for regulation. The GAO also cited the concerns of state regulators regarding their ability to regulate utility holding companies.[18]

The Committee convened a hearing regarding PUHCA reform on June 14 and 15, 1983, but took no further action during that legislative session.

During the 20-year debate on PUHCA reform, Congress successfully enacted piecemeal amendments to the Act to respond to the changing dynamics of the energy industry. For example, in 1978, Congress adopted the "Public Utility Regulatory Policies Act" to exempt certain new energy generation facilities from PUHCA regulation. In 1986, Congress enacted the "Regulatory Fairness Act" that added additional protections to consumers who feared wholesale utility companies were including unjust charges in utility rates. In 1992, Congress enacted the "Energy Policy Act" to amend PUHCA and encourage competition in the wholesale energy market. In 1995, Congress enacted the "Telecommunications Act," which included a provision to encourage competition in the new telecommunications industry by allowing registered holding companies to establish exempt telecommunications subsidiaries. While Congress created limited opportunities for utility holding company diversification with these amendments to PUHCA, it has not yet had the opportunity to accomplish comprehensive reform of the Act itself.

---

[15] CRS Report, "Electricity Restructuring Background: Public Utility Holding Company Act of 1935 (PUHCA)," Jan. 7, 1999 at 5.

[16] In 1981, three measures were introduced by Senators D'Amato and Johnston regarding PUHCA: S. 1869, a bill to amend the Public Utility Holding Company Act of 1935 to simplify its administration and to remove restrictions no longer necessary to the protection of investors and consumers; S. 1870, a bill to amend the Public Utility Holding Company Act of 1935 to improve financial performance in the electric and gas utility industries by removing unnecessary impediments to the exercise of sound and prudent business judgment by utility executives; and S. 1871 a bill to amend section 2 of the Public Utility Holding Company Act of 1935. (November 19, 1981, Congressional Record at 28357).

[17] Statement of Senator Alfonse D'Amato, November 19, 1981, Congressional Record at 28357.

[18] GAO Report, "Analysis of SEC's Recommendation to Repeal the Public Utility Holding Company Act," GAO/RCED–83–118, August 30, 1983, at I–v.

SEC study triggers new committee action

In 1994, the SEC began a comprehensive study of PUHCA. The study considered the effectiveness of the SEC's administration of PUHCA and examined initiatives for modernizing PUHCA in light of changes in the energy industry. In June 1995, the SEC's Division of Investment Management published a comprehensive report on the findings of the study, including the history of PUHCA, subsequent administrative and legislative changes to PUHCA, and the energy industry in general. The SEC report concluded that PUHCA has accomplished its basic purpose of protecting investors, simplifying the utility industry and preventing industry abuses. The report further concluded that PUHCA, in many respects, either duplicated other state or federal regulation or was no longer necessary to prevent the recurrence of the abuses that led to the statute's enactment.[19] Although the SEC had first made this same finding in 1981, in the 1995 report the SEC examined more closely the effect of PUHCA repeal on the FERC and states' ability to continue to protect consumers.

The SEC report recommended that Congress repeal PUHCA (subject to certain conditions) since "the current regulatory system imposes significant costs, indirect administrative charges and foregone economies of scale and scope, that often cannot be justified in terms of benefits to utility investors."[20] The SEC recommended that Congress retain certain PUHCA provisions, noting that otherwise consumers could be exposed to some of the same abuses that PUHCA was enacted to prevent. As SEC Commissioner Isaac C. Hunt, Jr. cautioned:

> There is a continuing risk that a monopoly, if left unguarded, could charge higher rates and use the additional funds to subsidize affiliated businesses in order to boost its competitive position in other markets. Thus, so long as electric and gas utilities continue to function as monopolies, the need to protect against this type of cross-subsidization will remain. . . . [T]he best means of guarding against cross-subsidization is likely to be audits of books and records and Federal oversight of affiliate transactions.[21]

The legislation reforming PUHCA

The 1935 act has become ineffective and burdensome

Although the SEC recommended Congress enact certain safeguards to protect consumers, it also outlined many of the ways PUHCA's burdensome regulation unnecessarily restricts the growth of the registered holding companies, the hundreds of exempt companies, and free-standing utility companies. As the SEC Study illustrates, developments in other areas of the law have rendered PUHCA obsolete. For example, PUHCA requires that holding companies make frequent disclosures and statements to the SEC. While these safeguards may have been necessary in 1935, the SEC can effectively protect investors through disclosures required under

[19] SEC Study, supra note 6, at 128–133.
[20] SEC Study, supra note 6, at x.
[21] Statement of Commissioner Isaac C. Hunt, Jr., supra note 2 at 6.

the Securities Act of 1933 and the Securities Exchange Act of 1934. PUHCA requires that the SEC review many acquisitions and mergers of utility and holding companies. The FERC also has jurisdiction to review and approve these transactions and in practice, the SEC generally defers to the FERC's decisions on competition issues.[22]

The Committee also heard testimony that PUHCA's restrictions preventing holding companies from owning utility subsidiaries that are not in the same geographic area may be an impediment to needed market protections and restructuring in California and across the United States. Also, this so-called integration requirement is outdated and a barrier to the production of efficient energy.[23] It has prevented at least one AAA bond rated holding company from investing in California's electricity generation and transmission infrastructure as the company feared it would have violated provisions under PUHCA.[24] The integration requirement may also prevent FERC from implementing key market power mitigation efforts called for in FERC Order 2000[25] such as the creation of independent regional transmission organizations (RTO).[26]

At its March 29, 2001 hearing, the Committee heard testimony that PUHCA may have marginally contributed to electricity shortages, price increases and rolling blackouts suffered by California utilities and rate payers during the 2000–2001 winter season by limiting the pool of investors that may have been interested in developing electricity generation and transmission in California. According to SEC Commissioner Hunt, "[PUHCA] certainly possibly could have limited the number of investors willing to go into the California scene."

---

[22] Most State commissions also have the authority to prevent mergers that are not in the "public interest." Thirty-three of forty-three State commissions responding to an SEC survey indicated that they have jurisdiction over utility mergers. Thirty responded that they regulate the acquisition of utility assets. (Written response to questions, Barry P. Barbash, Director, Division of Investment Management, Securities and Exchange Commission: "Hearing on the Public Utility Holding Company Act of 1995," Senate Committee on Banking, Housing and Urban Affairs, June 6, 1996 at 2.)

[23] In 1935, Congress believed that this "integration requirement" would improve regulation. For example, PUHCA prevents exempt holding companies from expanding and investing—exempt holding companies cannot diversify or acquire utilities interstate without falling under PUHCA's restrictive registration provisions. Senator J. Bennett Johnston, (D–LA), testified before the Committee about the burden that the geographic limitations impose: "PUHCA's outdated geographic restrictions don't just apply to a few large companies here and there. These geographic restrictions directly circumscribe the investment options of 75–80 percent of the investor-owned utility industry." (Testimony of Senator J. Bennett Johnston: "Hearing on the Public Utility Holding Company Act of 1995," Senate Committee on Banking, Housing and Urban Affairs, June 6, 1996 at 2.)

[24] Statement of David L. Sokol, Chairman and CEO, MidAmerican Energy Holding Company: "Hearing on the Public Utility Holding Company Act of 2001," Senate Committee on Banking, Housing, and Urban Affairs, Subcommittee on Securities and Investment, March 29, 2001 at 4–5. MidAmerican, is a diversified, international energy corporation headquartered in Des Moines, Iowa. MidAmerican is currently exempt from PUHCA because the majority of its utility holdings are located in one state. Had the company invested in California markets it would have been required to separate itself from its largest shareholder, Berkshire Hathaway.

[25] 95 FERC 61, 114.

[26] Statement of Cynthia A. Marlette, Deputy General Counsel, Federal Energy Regulatory Commission: "Hearing on "Public Utility Company Holding Act of 2001," Senate Committee on Banking, Housing, and Urban Affairs, Subcommittee on Securities and Investment, March 29, 2001 at 5–6. "It is RTOs that will provide the major structural reform needed in the electric industry to ensure mitigation of market power and an efficient, reliable transmission system . . . Under PUHCA, an entity that owns or controls facilities used for the transmission of electric energy—such as an RTO—falls within the definition of public utility company, and any owner of ten percent or more of such a company would be a holding company and potentially could be required to become a registered holding company. This could serve as a significant disincentive for investments in independent for-profit transcos that qualify as RTOs." Id.

The Committee considered the SEC report and agreed with its conclusion that: "[g]iven the developments in the industry and in other regulatory regimes, a less structural, more targeted regulatory approach now seems appropriate."[27] Mindful that consumers need protection from unfair rates, the Committee, in crafting S. 206, strengthened the ability of Federal and state regulators to protect consumers from unfair rate increases and drafted the bill to address any regulatory gaps opened up by PUHCA repeal so that regulators would have ample authority to protect consumers.

Protecting consumers from paying unfair rates

During the Committee's consideration of PUHCA repeal, the regulators, consumers, and industry groups identified as their primary concern that repeal could provide utility companies with the opportunity to finance diversification by increasing energy rates to utility customers. According to these groups, the parent holding company could fund the operation of its non-utility subsidiaries and its diversification through affiliate transactions. The parent company would then be able to subsidize such non-utility transactions and consumers would end up paying for the transaction through higher rates.[28]

Charles A. Acquard, Executive Director of the National Association of State Utility Consumer Advocates (NASUCA) testified to the Committee that the repeal of PUHCA before public utility companies are subject to effective competition, or effective regulation where effective competition does not exist, could leave consumers unprotected from artificially inflated prices caused by monopoly abuses by very large utility companies.[29] NASUCA also contends that the repeal or easing of restrictions on utility diversification will make it more difficult for regulators to track and allocate costs in order to prevent the cross-subsidization of the parent holding company's non-utility subsidiaries by overcharging ratepayers.[30]

NASUCA has concluded that if PUHCA were repealed today, neither the current state nor Federal regulatory scheme, nor the current state of competition, would be sufficient to protect consumers.[31] If PUHCA is repealed, NASUCA would like to see the continuation of the Act's restrictions on public utility holding company diversification into non-utility businesses and its regulations on capital structure.[32]

The Committee considered how to best ensure that the FERC and state regulators would be able to prevent the funding of non-utility investments through utility rates and other unfair affiliate transactions. The Committee followed the regulators' recommenda-

---

[27] SEC Study, supra note 6, at 133.

[28] During the Committee's 1996 hearing on PUHCA, this concern was most clearly stated in testimony by ELCON: "[t]he concern here is that the potential for self dealing, unfair cost allocation, and cross subsidization between regulated and unregulated affiliates to the detriment of the captive ratepayers of the regulated affiliate. * * * No captive ratepayers of a regulated entity—whether they be residential, small business, or large industrial consumers—should ever be forced to subsidize the unregulated, diversified investments of the regulated entity's parent company or any unregulated affiliate." (Testimony of John Hughes on behalf of ELCON: "Hearing on the Public Utility Holding Company Act of 1995," Senate Committee on Banking, Housing and Urban Affairs, June 6, 1996, at 7.)

[29] Statement of Charles A. Acquard: "Hearing on Public Utility Holding Company Act of 2001," Senate Committee on Banking, Housing, and Urban Affairs, Subcommittee on Securities and Investment, March 29, 2001 at 2 and 4.

[30] Id. at 5.

[31] Id at 8–9.

[32] Id. at 5.

tions to prevent unfair rates. To enable the FERC and the states to best protect consumers, the legislation would improve the regulators' ability to determine whether a public utility company may recover in rates costs associated with affiliate transactions.

The Committee also addressed concerns over the ability of companies to pass through costs to rate customers from affiliate transactions by affirmatively noting the existing role of FERC in regulating wholesale electricity rates. According to the FERC's testimony before the Committee, S. 206 would give the FERC authority to protect registered system ratepayers against these abusive affiliate contracts. FERC Deputy General Counsel Cynthia Marlette, testified that: "S. 206 provides an appropriate means to help promote emerging competitive electric power markets while at the same time providing the FERC and states additional access to books and records in order to protect consumers against inappropriate cross-subsidization and market power abuse."[33] The Committee accepted the FERC's assurance that it could protect consumers through the ratemaking process and adopted an amendment offered by Senators Enzi and Sarbanes, emphasizing the continuation of FERC's authority to require that jurisdictional rates are just and reasonable, including the ability to deny or approve the passthrough of costs and the prevention of cross-subsidization and the promulgation of such rules and regulations as are necessary or appropriate for the protection of utility consumers.

Indeed, prior to adoption of the Enzi-Sarbanes amendment, SEC Commissioner Hunt testified that "S. 206 represents * * * the type of conditional repeal that the SEC has endorsed. In particular, S. 206 would provide the FERC with the right to examine books and records of holding companies and their affiliates that are relevant to costs incurred by associate utility companies, in order to protect ratepayers. * * * S. 206 thus accomplishes many of the goals of the conditional repeal advocated by the SEC."[34]

Closing the Ohio Power gap

In order to ensure that the FERC and states have unqualified authority to disallow costs associated with certain affiliate transactions, S. 206 would solve the regulatory conundrum caused by a 1992 Court of Appeals decision, in *Ohio Power Company* v. *FERC,* 954 F.2d 779 (D.C. Cir. 1992). In *Ohio Power,* the court held that the SEC's approval of costs associated with an affiliate transaction under PUHCA preempted the FERC's determination of whether costs related to that transaction should be included in rates. As a result of *Ohio Power,* the FERC must allow costs approved by the SEC to be passed on to consumers through increases in utility rates, even if those costs exceed market value.

S. 206 would address the *Ohio Power* problem by increasing the energy regulators' ability to protect consumers. S. 206 would eliminate the *Ohio Power* regulatory gap by eliminating PUHCA and the conflicting jurisdiction over ratemaking between the SEC and the FERC. The legislation would explicitly grant authority to state and Federal regulators so that the regulator overseeing the ratemaking function has the final say as to whether costs associated

[33] Statement of Cynthia Marlette, supra note 26 at 8.
[34] Statement of Commissioner Isaac C. Hunt, Jr., supra note 2 at 7.

with an affiliate transaction may or may not be fairly passed on to consumers. The Committee does not intend the FERC to inherit the SEC's current authority to approve costs. Instead, the FERC's authority remains limited to wholesale ratemaking.

Expanding the regulators' access to company books and records

The Committee heard testimony from the regulators that the most important tool for regulators to keep companies from passing on non-utility costs to ratepayers is sufficient access to company books and records.

The SEC recommended that if PUHCA were repealed "Congress [must] ensure state access to books and records, and provide for federal audit authority and oversight of affiliate transactions." [35]

Cynthia Marlette also testified that "Congress should ensure that the FERC and state regulatory authorities have adequate access to the books and records of all members of all public utility holding company systems when that information is necessary to meet their statutory rate-making responsibilities." [36]

To address the regulators' concerns about books and records, the Committee included in S. 206 provisions to strengthen the regulators' authority to obtain records of all the companies in a holding company system.[37]

Section 5 of S. 206 permits the FERC to examine all books and records of a holding company and each of its subsidiaries and affiliates relevant to costs incurred by a utility company and as "necessary or appropriate for the protection of utility customers."

The Committee believes that state regulators must also have access to records of all companies in a holding company system no matter what kind of business they are involved in, in order to set rates, allocate costs, and guard against potentially abusive affiliate transactions.

According to the SEC Study, many states are unable to obtain readily the books and records of an out-of-state company.[38]

The groups representing manufacturers and consumers who testified before the Committee in the past raised concerns about the state commissions' inability to regulate the out-of-state utility operations of multistate companies. The Committee addressed these concerns in the legislation. Section 6 of S. 206 would grant to state commissions access to all the books and records of every company in a holding company system, no matter where that company is located, to the extent that the state commissions need such access to set consumer retail rates of a public utility in its jurisdiction. S. 206 also allows any Federal district court in a state to enforce that state commission's access to company books and records. In addition, Section 15 of S. 206 creates an inter-agency task force to review competition in the wholesale and retail markets for electricity. The task force must report its findings to Congress no later than one year after enactment of S. 206.

---

[35] SEC Study supra note 6, at 133–134.

[36] Statement of Cynthia Marlette, supra note 26 at 3.

[37] The legislation would give the FERC additional authority to access books and records of all companies in a holding company system. The Committee clarifies in section 9 of the legislation that access would supplement the FERC's existing ratemaking authority under section 301 of the Federal Power Act and section 8 of the Natural Gas Act.

[38] SEC Study, supra note 6, at 134.

NARUC testified in an earlier hearing that it was concerned that the exemption authority granted to the FERC in Section 7 not be construed to allow federal exemptions from state access to books and records.[39] The Committee continues to agree. Section 7 clearly limits FERC authority to grant exemptions from federal access to books and records under Section 5. The bill does not give FERC authority to exempt holding companies from state access to books and records under Section 6. Further, while the Committee intends for regulators to have access to books and records no matter where they are located in order to set rates, it does not intend for this authority to be used outside of a ratemaking context. The Committee expects regulators will not have any cause to access books and records of associate or subsidiary companies which do not engage in affiliate transactions or other business with the public utility.

A level playing field for all

Among other things, the Committee intends for this legislation to put all utility companies on a level playing field. This left the Committee to deal with the question of how to treat the formerly exempt holding companies. In 1997, FERC General Counsel Susan Tomasky suggested in her testimony to the Committee that legislation to repeal PUHCA include only narrow exemption provisions—which would grandfather previously approved activities and transactions but not exempt holding companies from affiliate abuse oversight.[40]

The NARUC, in an earlier hearing, expressed its concern that legislation not give the FERC authority to exempt companies from state books and records access. The NARUC testified to the Committee that "any legislation to reform the Holding Company Act should unequivocally establish an enforceable State right of access by States to all such books and records, wherever located, that directly or indirectly affect consumers. States' rights to secure access to books and records is critical for the effective oversight of out of state activities of multistate holding companies that affect utility rates."[41]

The Committee agrees with the regulators that all holding companies should be subject to similar regulation. As a result, S. 206 would allow a company to continue to engage in all activities and transactions in which it may currently engage. Further, all transactions and companies in the holding company system—whether currently registered or exempt—would be subject to the newly expanded Federal books and records provisions, unless the FERC finds that a transaction is not relevant to its ratemaking jurisdiction.

The Committee expects that holding companies which currently hold exemptions under section 3(a)(3) of PUHCA will petition the FERC and will be exempted from Section 5 of this Act as long as their public utility activities do not fall under the definition of jurisdictional rates set forth under this Act. Similarly, the Committee

---

[39] Statement of Robert Gee on behalf of NARUC: "Hearing on the Public Utility Holding Company Act of 1997," Senate Committee on Banking, Housing, and Urban Affairs, April 29, 1997 at 3–4.

[40] Statement of Susan Tomasky, General Counsel, FERC: "Hearing on the Public Utility Holding Company Act of 1997," Senate Committee on Banking, Housing, and Urban Affairs, April 29, 1997 at 3.

[41] Statement of Robert Gee, supra note 39 at 6.

expects that state access to the books and records of these holding companies will only be used to set the retail rates of public utilities which sell power to the public.

Companies that are holding companies only because they own any of three specialized energy companies (Exempt Wholesale Generators ("EWGs"), Foreign Utility Holding Companies ("FUCOs"), and/or Qualified Facilities ("QFs")) are exempted from the books and records provision of S. 206. The Committee recognized that these companies are not affiliated with public utilities so there is no possibility of affiliate abuse and no need for FERC access to affiliate books and records. However, if any of these holding companies acquires a public utility, it would lose its exemption. The Committee does not intend to change the Public Utility Regulatory Policies Act provisions regarding regulation of holding companies that hold solely QFs. To maintain current state regulation of QFs, the bill exempts companies that are holding companies solely by ownership of QFs from the state access to books and records provisions of Section 6. This exemption would not extend to a holding company which held QFs' as well as other public utility affiliates.

Market power

The Committee heard testimony that with PUHCA repeal companies would merge to form large utility holding company systems. The effect of these mergers would be to reduce the number of companies entering a deregulated market, thus limiting competition.[42]

Both state and Federal regulators addressed merger and diversification issues in their testimony. The Committee is satisfied that the regulators' authority to approve or disapprove mergers and the authority of states to set limits on diversification is sufficient to protect against market power abuses.

SECTION-BY-SECTION ANALYSIS

Section 1. Short title

Section 1 provides that the bill may be cited as the "Public Utility Holding Company Act of 2001."

Section 2. Findings and purposes

Section 2 sets out the findings and purposes of the Act. The "findings" of the Act state that the constraints placed on holding company systems by the Public Utility Holding Company Act of 1935 (the "1935 Act") are not needed but that there is continuing need for limited Federal and state regulation to protect the ratepayers of electric utilities and natural gas companies. The "purpose" of the Act is to eliminate unnecessary regulation through repeal of the 1935 Act, while facilitating effective state and Federal rate regulation by assuring access to holding company system books and records that are relevant to setting utility rates.

Section 3. Definitions

Section 3 defines the terms used in the Act. The definitions of "affiliate," "associate company," "company," "electric utility company," "gas utility company," "holding company," "public utility

[42] Statement of Commissioner Isaac C. Hunt, Jr., supra note 2 at 7; statement of Charles A. Acquard, supra note 29 at 7.

company," "state commission," "subsidiary company" and "voting security" are taken from the definitions in Section 2 of the Public Utility Holding Company Act of 1935, 15 U.S.C. § 79b(a). The Act preserves the "10 percent or more" threshold used by the 1935 Act to define a "holding company" and a "subsidiary company". As in the 1935 Act, the alternative definition for these two terms (the determination by the regulator that a "controlling influence" exists) is also used.

The terms "exempt wholesale generator" and "foreign utility company" have the same meaning as in sections 32 and 33, respectively, of the 1935 Act as those sections existed on the day before the effective date of this Act. These terms were added to the 1935 Act by Title VII of the Energy Policy Act of 1992.

The terms "jurisdictional rates", "natural gas company" and "public utility" are taken from the Natural Gas Act and the Federal Power Act. Specifically, the term "natural gas company" tracks the language of Section 2(6) of the Natural Gas Act, 15 U.S.C. § 717a(6). The term "public utility" tracks that of Section 201(e) of the Federal Power Act, 16 U.S.C. § 824(e). The term "jurisdictional rates" is intended to encompass the full ratemaking jurisdiction of the Federal Energy Regulatory Commission's authority to set rates under the Federal Power and Natural Gas Acts.

Section 4. Repeal of the Public Utility Holding Company Act of 1935

Section 4 repeals the 1935 Act.

Section 5. Federal access to books and records

Section 5 provides the Federal Energy Regulatory Commission authority to inspect such books and records of holding companies, associate companies, subsidiary companies and affiliate companies as the Commission deems relevant to its ratemaking responsibilities under the Federal Power and Natural Gas Acts. To this end, companies are required to maintain and make available to the Commission such books, accounts, memoranda and other records as the Commission deems relevant to rate setting. The Commission's authority under this section supplements its authority over books and records under the Federal Power and Natural Gas Acts.

This section imposes a confidentiality requirement taken from the confidentiality requirement in section 301(a) of the Federal Power Act. Consistent with current practice under the FPA, except as may be directed by the Commission or the courts, no member, officer, or employee of the Commission may divulge facts or information obtained during the course of examinations authorized under this section.

Section 6. State access to books and records

Section 6 provides state regulatory commissions authority to inspect books, accounts, memoranda, and other records of a public utility holding company or associate or affiliate companies as may be relevant to costs incurred by an electric utility company or a gas utility company necessary to carry out state regulation of public utility companies in a holding company system. The authority is to be exercised by written request and subject to such terms and conditions as are necessary and appropriate to safeguard against un-

warranted disclosure to the public of any trade secrets or sensitive commercial information.

Any company which is a holding company solely because it holds Qualifying Facilities under Public Utility Regulatory Policies Act ("PURPA") is exempt from the books and records provision. This exemption is intended to preserve the current regulatory structure under which these companies operate.

The rights of the states under this section are enforceable in Federal district court.

The authority granted by Section 6 is intended to supplement existing state authority over holding company systems, not to expand or limit any existing authority a state commission has to regulate a public utility. To ensure this result, Section 6 provides that it does not preempt applicable state law concerning access to business information or in any way limit the rights of a state to obtain books, records, or other information under Federal law, contract, or otherwise. Some of these rights are set out in Section 201(g) of the Federal Power Act, 16 U.S.C. § 824(g).

Section 7. Exemption authority

Section 7 provides the Commission authority to exempt certain entities from the requirements of Section 5, with respect to access to books and records and requires the exemption of certain entities from those requirements.

Section 7(a) requires the Commission, not later than 90 days after the effective date of this act, to issue a final rule exempting from the requirements of Section 5 any person that is a holding company solely by reason of owning one or more (a) qualifying facilities (QFs); (b) exempt wholesale generators (EWGs); (c) foreign utility companies; or (d) any combination thereof.

The purpose of this provision is to ensure that businesses whose activities are solely limited to ownership of these categories of generation investment will not be subject to the requirements of Section 5. In addition, the Commission may by rule or order exempt any person or class of transactions from the requirements of Section 5 if it finds that the books, records, accounts, memoranda or other records or class of transactions are not relevant to the jurisdictional rates of a public utility or natural gas company.

Section 8. Affiliate transactions

Section 8(a) clarifies that the Commission's authority to require that jurisdictional rates are just and reasonable, including the ability to approve or deny the pass-through of costs, the prevention of cross-subsidization, and the promulgation of rules necessary or appropriate for the protection of utility customers, are not affected by the Act.

Section 8(b) makes explicit that nothing in the Act precludes the Commission or a state commission from determining under otherwise applicable law whether a public utility company, natural gas company, or a public utility may recover in rates any costs of an activity performed by an associate company, or any costs of goods or services acquired by the public utility company from an associate company.

Section 9. Applicability

Section 9 makes clear that, unless specifically provided in the Act, the Act does not apply to the United States, a state or any political subdivision of a state, any foreign governmental authority not operating in the United States, or any agency, authority, instrumentality, officer, agent or employee of these entities.

Section 10. Effect on other regulations

Section 10 provides that nothing in this Act precludes the Commission or a state commission from exercising its jurisdiction under otherwise applicable law to protect gas and electric utility consumers from paying too much for goods and services provided by associate companies and from cross subsidization of associate companies by regulated public utility companies.

Section 11. Enforcement

Section 11 refers to authorities contained in the Federal Power Act to provide the Commission full authority to enforce the provisions of the Act. These authorities include the authority: (i) to receive and proceed on complaints; (ii) to investigate any facts, conditions, practices or matters necessary to determine whether there has been a violation of the Act or any rule, regulation or order issued under the Act; and (iii) to hold hearings. Section 11 also gives the Commission authority to implement rules of practice and procedure and to perform any and all acts necessary to carry out the provisions of the Act.

Section 12. Savings provisions

Section 12 provides that, in general, nothing in the Act prohibits a person from engaging in activities or transactions in which it is legally engaged or authorized to engage on the date of enactment.

This savings provision ensures that prior authorizations made by the Securities and Exchange Commission and the Federal Energy Regulatory Commission continue in force under this Act. However, this Section is also intended to ensure that companies are not bound by previously ordered limits on activities when the activities would otherwise be allowed by this Act.

This section also provides that nothing in the Act limits the authority of the Commission under the Federal Power Act (including section 301 of that Act) or the Natural Gas Act (including section 8 of that Act).

Section 13. Implementation

Section 13 requires the Commission to promulgate such regulations as may be necessary or appropriate to implement the provisions of this Act, except for provisions pertaining to state access to books and records. These regulations are to be promulgated not later than eighteen months after the date of enactment.

Section 13 also requires the Commission to submit a report to Congress detailing technical and conforming amendments to Federal law necessary to implement the provisions of this Act. This report is required eighteen months after the date of enactment.

Section 14. Transfer of resources

Section 14 provides for the transfer of relevant books and records from the Securities and Exchange Commission to the Federal Energy Regulatory Commission.

Section 15. Inter-agency review of competition in the wholesale and retail markets for electric energy

Section 15 establishes the Electric Energy Market Competition Task Force, comprised of appointees from the Department of Justice, the Federal Energy Regulatory Commission, the Federal Trade Commission, the Department of Agriculture's Rural Utility Service, and the Securities and Exchange Commission. The task force is required to report to Congress within one year following the date of enactment on competition in the wholesale and retail markets for electric energy.

Section 16. GAO study on implementation

Section 16 requires the GAO to report to the Congress no later than 24 months following the date of enactment of the Act on the effectiveness of the Federal Government and the states to (1) prevent anti-competitive practices by public utility holding companies; and (2) promote competition and efficient energy markets to the benefit of consumers.

Section 17. Effective date

Section 17 provides that the Act shall take effect 18 months after date of enactment.

Section 18. Authorization of appropriations

Section 18 authorizes to be appropriated funds necessary to carry out the Act.

Section 19. Conforming amendments

This section repeals section 318 of the Federal Power Act, 16 U.S.C. 825q. This section recognizes that repealing the 1935 Act will eliminate any concerns about the possibility of conflicting decisions of the Securities and Exchange Commission and the Federal Energy Regulatory Commission.

REGULATORY IMPACT STATEMENT

In accordance with Paragraph 11(g), rule XXVI of the Standing Rules of the Senate, the Committee makes the following statement regarding the regulatory impact of the bill.

The chief effect of the legislation will be to eliminate the role of the Securities and Exchange Commission for administration of the Public Utility Holding Company Act, and invest remaining duties under the Public Utility Holding Company Act of 2001 in the Federal Energy Regulatory Commission. It is expected that this will result in a net reduction in regulatory burden.

CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

Senate rule XXVI, Section 11(b) of the Standing Rules of the Senate, and Section 403 of the Congressional Budget Impoundment and Control Act, require that each committee report on a bill con-

taining a statement estimating the cost of the proposed legislation, which was prepared by the Congressional Budget Office. The Congressional Budget Office Cost Estimate and its Estimate of Costs of Private-Sector Mandates, both dated April 24, 2001, are hereby included in this report.

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, May 1, 2001.

Hon. PHIL GRAMM,
Chairman, Committee on Banking, Housing, and Urban Affairs, U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for S. 206, the Public Utility Holding Company Act of 2001.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contacts are Lisa Cash Driskill and Ken Johnson (for federal costs), Victoria Heid Hall (for the state and local impact), and Lauren Marks (for the private-sector impact).

Sincerely,

BARRY B. ANDERSON
(For Dan L. Crippen, Director).

Enclosure.

S. 206—Public Utility Holding Company Act of 2001

Summary: The bill would repeal the Public Utility Holding Company Act and assign certain new responsibilities to the Federal Energy Regulatory Commission (FERC). CBO estimates that enacting S. 206 would reduce the need for appropriated funds for the Securities and Exchange Commission (SEC) by about $2 million in fiscal year 2003 and by about $3 million a year thereafter. Any additional costs imposed on the FERC would be offset by user fees the agency is mandated to charge to industries it regulates. S. 206 also would require the General Accounting Office (GAO) and an interagency task force to perform studies on competition within the electricity industry. Subject to the availability of appropriated funds, CBO estimates such studies would cost about $500,000 over the 2002–2003 period.

The bill would not affect direct spending or receipts, so pay-as-you-go procedures would not apply. S. 206 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA).

Estimated cost to the Federal Government: Section 4 would repeal the Public Utility Holding Company Act, effective 18 months following enactment of S. 206. Based on information from the SEC, CBO estimates that this repeal would reduce the agency's costs by about $2 million in fiscal year 2003 and by about $3 million a year thereafter, assuming the necessary appropriation action. Discretionary savings would total about $11 million over the 2002–2006 period.

Section 5 would authorize the FERC to have access to any records of public utilities and natural gas companies that are necessary for the commission to protect utility customers with respect to interstate transactions involving electricity and natural gas.

Based on information from the FERC, CBO estimates this activity would cost the agency about $3 million annually starting in 2003. This amount would be offset by fees that the agency is required to charge the industries it regulates. Therefore, the new responsibilities that the bill would create for the FERC would have no net budgetary impact.

The bill also would require the establishment of an interagency task force that would review competition within the electricity industry and report to the Congress within one year. CBO estimates that this study would cost about $250,000, assuming the appropriation of the necessary amounts.

GAO would be required to perform a study on the success of the federal government and the states in preventing anticompetitive practices and promoting competition within the electricity industry. Such a report would be due to the Congress between 18 and 24 months following the bill's enactment. Based on information from GAO, CBO estimates that completing this study would cost about $250,000, assuming appropriation of the necessary amounts.

The effects of this legislation fall within budget functions 270 (energy) and 370 (commerce and housing credit).

Pay-as-you-go considerations: None.

Estimated impact on state, local, and tribal governments: S. 206 contains no intergovernmental mandates as defined in UMRA. States could incur costs, however, if they choose to issue new regulations or enact new legislation to fill any regulatory gaps created by the repeal of the Public Utility Holding Company Act.

Estimated impact on the private sector: S. 206 would impose no new private-sector mandates as defined in UMRA. The bill would transfer regulatory authority for certain business-related transactions of public utility holding companies from the Securities and Exchange Commission to the Federal Energy Regulatory Commission.

Estimate prepared by: Federal Costs: Lisa Cash Driskill and Ken Johnson. Impact on State, Local, and Tribal Governments: Victoria Heid Hall. Impact on the Private Sector: Lauren Marks.

Estimate approved by: Peter H. Fontaine, Deputy Assistant Director for Budget Analysis.

CHANGES IN EXISTING LAW

In the opinion of the Committee, it is necessary to dispense with the requirement of Section 12 of rule XXVI of the Standing Rules of the Senate in order to expedite the business of the Senate.

ADDITIONAL VIEWS

Efforts at opening a dialogue with the opposing views on S. 206, the Public Utility Holding Company Act of 1935 (PUHCA), have shown that a mutually-agreeable solution is not inconceivable and is highly possible. The only limitations that remain would involve intractability on the part of one or more of the negotiating participants.

Congress has not concurred outside of the interests of the committee of jurisdiction for the past 20 years over PUHCA repeal. Significant opposition raised by the rural electric cooperatives and the public power organizations including municipal power authorities, has proved successful enough to block almost every legislative effort to move the bill beyond passage out of the Senate Committee on Banking, Housing, and Urban Affairs. Problems in California's electric market, rising fuel costs, an aging electricity infrastructure, and threats to international energy supplies have drawn national attention to the absence of a comprehensive energy policy. This heightened awareness of our energy needs has renewed interest in providing wholesale and retail electric energy markets with the tools necessary to address the United States' energy demands in the 21st Century.

At a March 29, 2001 hearing on S. 206, the Public Utility Holding Company Act of 2001, before the Senate Banking Subcommittee on Securities and Investments which I chair, several witnesses testified that PUHCA's antiquated and redundant regulations have barred companies and investors from investing in upgrades for California's electricity infrastructure. Cynthia Marlette, the Federal Energy Regulatory Commission's (FERC) Deputy General Counsel stated that PUHCA is also an impediment to entities being able to invest in independent regional transmission organizations (RTO), a market structure remedy that FERC believes is "the key to mitigating the major market power of vertically-integrated electric utilities, improving reliability of the transmission grid, and assuring more efficient use of our transmission facilities." (Statement of Cynthia A. Marlette, Deputy General Counsel, Federal Energy Regulatory Commission: Hearing on "Public Utility Company Holding Act of 2001," Senate Banking Subcommittee on Securities and Investment, March 29, 2001.)

In spite of these acknowledged obstacles to investment in the electric industry, and PUHCA repeal endorsements by both FERC and the Securities and Exchange Commission (SEC), PUHCA repeal opponents have consistently opposed PUHCA legislation based on a policy that PUHCA repeal should not occur without adequate market protections in place to fill the void created in a PUHCA-free energy market. Charles A. Acquard, Executive Director of the National Association of State Utility Consumer Advocates (NASUCA) testified that "NASUCA urges Congress and the SEC

not to take any action that would weaken [PUHCA] without first ensuring that public utility holding companies are either subject to effective competition or subject to effective regulation, where effective competition does not yet exist or where competition would not induce efficiency, reduce costs and advance consumer interests. . . . We conclude that, if PUHCA were repealed today in the manner proposed in S. 206, neither the remaining regulatory scheme nor the current state of competition would be sufficient to protect consumers." (Statement of Charles A. Acquard, NASUCA Executive Director: Hearing on "Public Utility Company Holding Act of 2001," Senate Banking Subcommittee on Securities and Investment, March 29, 2001.) These clearly defined position statements make it apparent that any successful effort to repeal PUHCA must include an attempt to resolve the concerns of PUHCA opponents.

Past negotiation efforts failed, in part, due to an uncompromising position assumed by PUHCA repeal opponents. The rural electric cooperatives and public power groups recognized that Congress' general lack of interest in repealing PUHCA did not require them to come to the table with reasonable demands that would satisfy their conditions that adequate market protections be created to protect consumers from possible holding company abuses. This year, however, these groups recognized that Congress' heightened awareness of electric energy issues, like PUHCA repeal, has created an atmosphere where it is in their best interest to cooperate in developing any possible changes to the national electricity market place.

The threat of California's ongoing problems, coupled with concerns over nationwide electric rate increases and possible delivery disruptions, set the stage for the PUHCA repeal opponents to come to the negotiating table with a much more reasonable list of demands. Some of the concerns raised by PUHCA repeal opponents include: Providing adequate FERC oversight of public utility mergers and acquisitions; giving FERC authority to impose structural solutions to address competition and unfair practices in national energy markets; creation of an inter-agency task force to study competition in the wholesale and retail electric energy markets; providing equitable civil penalties for public utilities across FERC's jurisdiction; and providing Federal oversight of sales and transfers of generation assets by public utilities.

Further discussions with the investor owned utilities supporting PUHCA repeal have revealed that PUHCA repeal proponents continue to be willing to discuss areas of difference with the opponents of this issue and that significant progress is possible in addressing these remaining issues. Because of jurisdictional issues raised by the Committee that amending the Federal Power Act would cause S. 206 to be referred to the Senate Committee on Energy and Natural Resources, the decision was made to address only those items that clearly would fall under the Banking Committee's jurisdiction. I offered an amendment to S. 206 that would create an inter-agency task force, to be made up of representatives from the Federal Energy Regulatory Commission, the Department of Justice, the Federal Trade Commission, the Securities and Exchange Commission, and the United States Department of Agriculture's Rural Utility Service, that would report back to Congress in one year with

a study that would review all aspects and participants in the national electric energy market. The examination would specifically look at: (1) the best means of protecting competition within the wholesale and retail electric market; (2) activities within the wholesale and retail electric market that may allow unfair and unjustified discriminatory and deceptive practices; (3) activities within the wholesale and retail electric market, including mergers and acquisitions, that deny market access or suppress competition; (4) cross subsidization that may occur between regulated and nonregulated activities; and (5) the role of state public utility commissions in regulating competition in the wholesale and retail electric market.

Included in the study amendment was a second degree amendment, cosponsored by the Banking Committee's Ranking Member, Senator Paul S. Sarbanes, that would draw attention to concerns raised by several members of the Committee regarding cross subsidization and the possibility that utility holding companies could pass through unfair and unreasonable costs to consumers, particularly when those costs have no business being included in electricity rates. The amendment put FERC on notice that Congress was aware of its oversight responsibilities and reaffirmed FERC's authority under the Federal Power Act to require that jurisdictional rates are just and reasonable, and that the agency has the ability to deny or approve the passthrough of costs and to prevent cross subsidization between holding company affiliate companies. The agency is expected to act in a responsible manner when it considers the expenses consumers are forced to pay in their monthly power bills.

The formation of the inter-agency task force and its subsequent study is an important first step in resolving the concerns of PUHCA repeal opponents. The remaining issues that must still be considered, namely Federal oversight of mergers and acquisitions and generation asset sales, and the authority of the FERC to require structural remedies in the case of anti-competitive and unfair conditions in electric markets, must still be negotiated and agreed to by both sides of this issue.

I am convinced that it is possible to reach a final agreement regarding PUHCA repeal during this Congress that addresses competition and consumer protection. This agreement, however, will require PUHCA repeal opponents to continue working in good faith, and for PUHCA repeal supporters to continue looking at new ways to address the concerns of their opponents in a way that adequately protects electricity consumers.

MIKE ENZI.

ADDITIONAL VIEWS OF SENATORS MIKE ENZI AND PAUL SARBANES

We offered an amendment to S. 206 to address the problem of cross-subsidization. The Committee adopted this amendment by voice vote. We want to explain briefly the rationale underlying this amendment.

Cross-subsidization was a major concern before PUHCA was enacted in 1935. With the prospect of PUHCA repeal, questions have been raised about the potential for cross-subsidization abuses. SEC Commissioner Isaac Hunt on page 8 of his written testimony on March 29, 2001, drew specific attention to the "types of abuses [that] can occur through affiliate transactions that cross-subsidize unregulated businesses with the profits of regulated utilities" and highlighted the need for regulators to "analyze all transactions within a holding company system and prohibit those that pose unreasonable risks for utility ratepayers."

The utility industry said that it does not want or intend cross-subsidization to occur. Mr. David L. Sokol, Chairman and CEO of MidAmerican Energy Holdings Company, a utility industry witness, stated in oral testimony on March 29, 2001, "I don't think there's any concern or real issue about cross-subsidization. And by the way, it should be completely prohibited. We have no interest in the consumer paying more than they should."

Our amendment affirms that nothing in S. 206 limits the FERC's authority under the Federal Power Act to require that jurisdictional rates are just and reasonable, including the ability to deny or approve the pass-through of costs, the prevention of cross-subsidization and the promulgation of such rules and regulations as are necessary or appropriate for the protection of utility consumers.

This authority is designed to prevent cross-subsidization abuses in the future, when PUHCA is no longer in force. Examples of abuses that have occurred in the past, which the Securities and Exchange Commission brought to our attention include:

Holding companies—

- Charging all of their rent and other office expenses to utility subsidiaries;
- Allocating to a utility subsidiary the entire cost of building a new headquarters for the holding company system rather than proportionally allocating costs to all companies in the system;
- Allocating all or most legal costs of the holding company system only to utilities rather than apportioning some costs to itself;
- Allocating all or most advertising costs of the holding company to utility subsidiaries instead of proportionally allocating costs to all companies in the system;

- Allocating all merger and acquisition costs relating to the formation of a new holding company to the utility subsidiaries rather than proportionally allocating costs to all companies in the system;
- Lending money to utility subsidiaries at interest rates higher than the utilities could obtain commercially;
- Demanding dividend payments to the holding companies that are in excess of current earnings of the utilities and that result in the utilities having a higher cost of borrowing and a reduced capacity to meet their operating obligations; and
- Allocating all of their tax liabilities to utility subsidiaries.

It is our intent that the FERC prevent cross-subsidization abuses in the future.

MIKE ENZI.
PAUL SARBANES.

○